Supreme Court, U.S.
FILED
OCT 7 1992
OFFICE OF THE CLERK

No. 92-319

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

BOARD OF COUNTY COMMISSIONERS OF SAN JUAN COUNTY,

Petitioner,

v.

LIBERTY GROUP, A California Limited Partnership; NORMAN ANDREW GURLEY; LIBERTY PARTNERS, INC., A California Corporation; F.M.G. PARTNERS, A California General Partnership; CHESTER ARTHUR WALKER, JR.; DOYLE LAVERNE HOLMES; ROBERT CLAYTON HOLMES; STEVE RAY HOLMES; LIBERTY CAPITAL MARKETS, INC., A California Corporation; PRUDENTIAL-BACHE SECURITIES, INC., A Delaware Corporation,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

---

PETITIONER'S REPLY BRIEF

J. M. DURRETT, JR.
San Juan County Attorney
112 S. Mesa Verde
Aztec, NM 87410
(505) 334-9481

JAMES L. DOW *
DOW LAW OFFICE, P.A.
P. O. Box 128
Carlsbad, NM 88221
(505) 885-2185

* Counsel of Record

Attorneys for Petitioner

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

BEST AVAILABLE COPY

QUESTIONS PRESENTED

1. Whether a limited partnership can associate with, or be employed by, itself under 18 U.S.C. § 1962(c), Racketeering Influenced Corrupt Organizations Act ("RICO"), so that the limited partnership may be both the RICO "person" and the RICO "enterprise".

2. Was the Tenth Circuit correct in concluding that the trial court's scienter instruction improperly allowed liability under Rule 10(b)-5 (promulgated under the Securities and Exchange Act of 1934, 17 C.F.R. Section 240) for merely negligent conduct, and in concluding that respondents properly objected to the instruction.

LIST OF PARTIES

Board of Commissioners of San Juan County, Petitioner

Liberty Group, A California Limited Partnership, Respondent

Norman Andrew Gurley, Respondent

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
LIST OF PARTIES	ii
REASONS FOR GRANTING THE WRIT	1
THE DISTRICT COURTS AND CIRCUIT COURTS ARE IN CONFLICT WHETHER THE PERSON MUST BE DISTINCT FROM THE ENTERPRISE UNDER RICO § 1962(a) AND § 1962(c)	1
CONCLUSION	8

TABLE OF AUTHORITIES

CASES — Page

United States Supreme Court:

Sedima, S.P.R.L. v. Imrex Co., Inc., 473 U.S. 479 (1985) 6

United States v. Turkette, 452 U.S. 589 7

United States Court of Appeals

Bennett v. United States Trust Co., 779 F.2d 397 (7th Cir. 1985) 4, 6

Board of County Commissioners of San Juan County v. Liberty Group, et al., 965 F.2d 879 (10th Cir. 1992) 7

Garbade v. Great Divide Mining and Milling Corp., 831 F.2d 212 (10th Cir. 1987) 2, 3, 5

Haroco v. American National Bank & Trust Co. of Chicago, 747 F.2d 384 (7th Cir. 1984) 3, 4, 6

B. F. Hirsch v. Enright Refining Co., 751 F.2d 628 (3rd Cir. 1984) 4, 6

Masi v. Ford City Bank and Trust Co., 779 F.2d 397 (7th Cir. 1985) 4, 6

Schofield v. First Commodity Corp. of Boston, 793 F.2d 28 (1st Cir. 1986) 3, 6

Schreiber Distributing Co. v. Serv-Well Furniture Co., 806 F.2d 393 (9th Cir. 1986) 3, 6

United States v. Computer Sciences Corp., 689 F.2d 1181 (4th Cir. 1982) 3

United States v. Hartley, 678 F.2d 961 (11th Cir. 1982) 8

United States District Court:

The Bruss Co. v. Allnet Communications Services, 606 F. Supp. 401 (N.D. Ill. 1985) 4

U. S. v. Benny, 559 F. Supp. 264 (N.D. Ca. 1983) 7

STATUTES

18 U.S.C. § 1961(4) 2

18 U.S.C. § 1962(a) 1, 3, 4, 7

18 U.S.C. § 1962(c) ..... i, 2, 3, 4, 7

CODE OF FEDERAL REGULATIONS

17 C.F.R. 240.10b-(5)(b) i

TABLE OF AUTHORITIES—Continued

Page

ADMINISTRATIVE PROCEEDINGS

Dist. Conduct Committee For District No. 25 v. *Liberty Capital Markets, Inc., et al.*, N.L.R.B. Complaint No. LA-4248 5

In Re Transamerica Securities, Inc., S.E.C. Administrative Proceeding No. 3-5810 5

LAW REVIEW

65 Boston U. L. Rev. 561 (1985) 4

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

No. 92-319

BOARD OF COUNTY COMMISSIONERS OF SAN JUAN COUNTY,

Petitioner,

v.

LIBERTY GROUP, A California Limited Partnership; NORMAN ANDREW GURLEY; LIBERTY PARTNERS, INC., A California Corporation; F.M.G. PARTNERS, A California General Partnership; CHESTER ARTHUR WALKER, JR.; DOYLE LAVERNE HOLMES; ROBERT CLAYTON HOLMES; STEVE RAY HOLMES; LIBERTY CAPITAL MARKETS, INC., A California Corporation; PRUDENTIAL-BACHE SECURITIES, INC., A Delaware Corporation,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

---

PETITIONER'S REPLY BRIEF

REASONS FOR GRANTING THE WRIT

THE DISTRICT COURTS AND CIRCUIT COURTS ARE IN CONFLICT WHETHER THE PERSON MUST BE DISTINCT FROM THE ENTERPRISE UNDER RICO § 1962(a) AND § 1962(c).

Section 1962(a) makes it unlawful "for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity . . . to

use or invest, directly or indirectly, any part of such income, or proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce. . . ."

Section 1962(c) makes it unlawful "for any person employed by or associated with any enterprise . . . to conduct or participate in the conduct of such enterprise's affairs through a pattern of racketeering activity. . ."

Section 1961 defines the term "enterprise": "As used in this chapter— . . . (4) 'enterprise' includes any individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity; . . ."

From a reading of these three sections of RICO, the language of the statute with regard to the meaning of the term "enterprise" is in conflict.

The Trial Court identified the enterprise as Respondent Liberty Group and overruled Respondent's Motion for JNOV. One of the grounds for Respondent's motion was that the person and enterprise must be distinct. Joint App. at 307. The Tenth Circuit reversed the Trial Court's RICO decision, holding: "The required separation between the RICO Enterprise and the Defendant Liberty Group was not established and JNOV should have been granted to Liberty Group as to any liability under Section 1962(c). Appendix A, P. 15a.

The record is replete with evidence that the enterprise Liberty Group received all of the monies the County was defrauded of, and Liberty Group conducted or participated in the affairs of the enterprise through a pattern of racketeering activity and the jury so found. Joint App. P. 299.

The Tenth Circuit's decision in the case at bar is in direct conflict with its earlier case of *Garbade v. Great Divide Mining and Milling Corporation*, 831 F.2d 212

(10th Cir. 1987). The Tenth Circuit, in *Garbade*, id., stated:

> "Section 1962(c) makes it unlawful for a 'person' to enter the activities of an 'enterprise' using racketeering activities. References are to 'employed by' and 'associated with'. The section does not relate to corporate or enterprise liability. *Schofield v. First Commodity Corp.*, 793 F.2d 28 (1st Cir.); *Haroco, Inc. v. American National Bank & Trust Co.*, 747 F. 2d 384 (7th Cir.); *United States v. Computer Sciences Corp.*, 689 F.2d 1181 (4th Cir.).
>
> There is no indication whatever that the corporation was in any way benefited by the alleged acts of the defendant. The existence of such benefits have provided in several cases an exception to this conclusion and to impose corporate liability under § 1962(a). . . .
>
> The 'person' and 'enterprise' combination liability can only occur when the corporation actually is the direct beneficiary of the pattern of racketeering activity. *Haroco, Inc. v. American National Bank & Trust Co.*, 747 F. 2d 384 (7th Cir.) (; also where it is to disgorge illegally obtained proceeds of illegal activities, *Schreiber Distributing Co. v. Serv-Well Furniture Co.*, 806 F.2d 393 (9th Cir.).
>
> In the case before us, the defendant corporation received no illegally obtained funds as contemplated by the statute. Its dismissal by the trial court was proper."

Thus, the Tenth Circuit is in direct conflict with its own decisions on this very question. Other circuits are also in conflict with this decision, namely, *Schofield v. First Commodity Corp.*, 793 F.2d 28 (1st Cir. 1986). In *Schofield*, id., the court in discussing the conflicting views resulting from the conflicting legislative language in 1962(a) and 1962(c) the court reasoned:

> "The language in section 1962(a) does not require a relationship between the person and the enterprise as

does section 1962(c), and so it does not require the involvement of two separate entities. Applied to the facts of this case, section 1962(a) would prohibit FCCB, the person, from using ill-gotten gains in FCCB, the enterprise. In contrast, section 1962(c) requires that the culpable person be 'employed by or associated with' an enterprise; we think it stretches the language too far to suggest that a corporation can be employed by or associated with itself. This approach to the two subsections

> 'thus makes the corporation-enterprise liable under RICO when the corporation is actually the direct or indirect beneficiary of the pattern of racketeering activity, but not when it is merely the victim, prize, or passive instrument of racketeering. This result is in accord with the primary purpose of RICO, which, after all, is to reach those who ultimately profit from racketeering, not those who are victimized by it.' Haroco, 747 F.2d at 402.

See also Masi v. Ford City Bank and Trust Co., 779 F.2d 397, 401-402 (7th Cir. 1985); Bennett v. United States Trust Co. of New York, 770 F.2d at 315 (2d Cir. 1985); B. F. Hirsch v. Enright Refining Co., 751 F.2d 628, 633-34 (3d Cir. 1984); The Bruss Co. v. Allnet Communication Services, 606 F. Supp. 401, 407 (N.D. Ill. 1985).[2]

---

[2] We recognize that funneling corporate liability into subsection (a) may affect plaintiffs in ways other than simply in the drafting of the complaint under one subsection rather than another. See Note, Judicial Efforts to Redirect an Errant Statute: Civil RICO and the Misapplication of Vicarious Corporate Liability, 65 Boston U. L. Rev. 561, 596-598 (1985). For example, subsection (a) requires a showing of the source of income and proof that funds were channeled into the corporation. It also covers only wrondoing involving money. But if neither section 1962(a) nor section 1962(c) cover all methods of corporate wrongdoing, it is up to Congress, and not the courts, to expand the scope of the statute. We rely on section 1962(a) only to show that our reading of section 1962(c) does not insulate corporations from all liability."

Liberty Group hid the $208,000.00 fraud it perpetrated upon San Juan which was not discovered until the New Mexico State Auditor discovered the fraudulent transactions. Liberty Capital Markets, Inc., the successor-in-interest to Liberty Group, Appendix A at P. 4a-5a.[1] Acting through its President, Doyle Holmes, Liberty Group refused to return the $208,000 and tried to mislead the San Juan County into believing the adjusted trades were not fraudulent transactions, *In Re Transamerican Securities, Inc.*, S.E.C. Administrative Proceeding No. 3-5810, and that the SEC, the NASD, and the New Mexico Securities Division had investigated the transactions and these government entities had never apprised Liberty Group of any irregularities or illegality in the manner in which these trades were conducted. Plaintiff's Exhibit No. 47, admitted into evidence, Tr. Vol. III, Pages 121-123. As a result of these investigations, NASD censured Gurley and Liberty Capital Markets, the successor corporation to Liberty Group, in a companion investigation of similar adjusted trades with Bernalillo County, New Mexico. *District Conduct Committee For District No. 25 v. Liberty Capital Markets, Inc., et al.*, N.L.R.B. Complaint No. LA-4248. The New Mexico Security Division, as a result of these investigations, censured the same defendants for the adjusted trades perpetrated not only on San Juan County, New Mexico, but on Bernalillo County, New Mexico and the City of Santa Fe, New Mexico.

Thus, this is a clear case that falls in the exception to the "person"—"enterprise" liability exceptions referred to in the Tenth Circuit's decision of *Garbade v. Great Divide Mining and Milling*, supra. Seven of the Circuit

[1] Liberty Capital Markets was incorporated as a California corporation and succeeded to all of the assets and liabilities of Liberty Group shortly before the County could bring suit to recover the $208,000 from Liberty Group and Liberty Capital Markets as a direct result of the fraudulent transactions.

Courts that have considered the exception to the 1962(a) "Person-Enterprise" rule have acknowledged the exception to the rule.[2]

The 7th Circuit speaking in *Masi v. Ford City Bank & Trust Co.*, supra, noted that the exception to the rule in *Haroco*, supra, was essentially dicta; however, the 7th Circuit adopted the reasoning in *Haroco*, supra, stating:

> "However, a corporation-enterprise may be held liable under subsection (a) when the corporation is also the perpetrator. As we parse subsection (a) a 'person' (such as a corporation-enterprise) acts unlawfully if it receives income derived directly or indirectly from a pattern of racketeering activity in which the person has participated as a principle within the meaning of 18 U.S.C. Section 2, and if the person uses the income in the establishment or operation of an enterprise affecting commerce. Subsection (a) does not contain any language in subsection (c) which suggests that the liable person and enterprise must be separate. . . . However, we adopt it as our holding because of the reasoning expressed in Haroco and because we find that this literal reading of the statute is in accord with the Supreme Court's approach in *Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. 479 (1985).

---

[2] Corporations who have used the racketeering practices and who have received the ill-gotten gains and benefited therefrom are excepted from the 1962(c) "person"—"enterprise" rule. As stated in *Haroco Inc. v. American National Bank & Trust Co.*, supra: The person enterprise liability can only occur when the corporation actually is the direct beneficiary of the pattern of racketeering activity. *Haroco, Inc. v. American National Bank & Trust*, supra. *Masi v. Ford City Bank & Trust Co.*, 779 F.2d 397 (7th Cir. 1985); *Bennett v. United States Trust Co. of NY*, 770 F.2d 315 (2nd Cir. 1985); *B. F. Hirsch v. Enright Refining Co.*, 751 F.2d 628 (3rd Cir. 1984); *Schreiber Distributing Co. v. Serv-Well Furniture Co.*, 806 F.2d 1393 (9th Cir.); *Schofield v. First Commodity Corporation of Boston*, 793 F.2d 28 (1st Cir. 1986).

Moreover, the interpretation that insulates the enterprise from liability under Section 1962(c) is not inconsistent with the remedial purposes of RICO. *United States v. Turkette*, 452 U.S. 589. A culpable enterprise may be held liable under another section of RICO 1962(a). The language in 1962(a) does not require a relationship between the person and the enterprise, as does 1962(c), and so it does not require the involvement of two separate entities. *Schofield v. First Commodity Corporation of Boston*, supra.

Applied to the facts of this case, Section 1962(a) would prohibit Liberty Group, the person, from using the ill-gotten gains in Liberty Group, the enterprise.

The Tenth Circuit in its decision in the case at bar further held:

> "With respect to the defendant Gurley, he may be a person under 1962(c). Thus, the defect in proving a 'person' separate from the 'enterprise' is not present with respect to Gurley and a new trial for such defect is not required."

The Tenth Circuit in its decision has given a free ride to the guilty party, Liberty Group, who perpetrated the fraud and received all its benefits and passed them on to Liberty Capital Markets, while placing the full brunt of RICO on the employee 'Gurley', all contrary to the intent of Congress. As stated in *U. S. v. Benny*, 559 F. Supp. 264 (N.D. Ca. 1983):

> "Hence, the person whose business was at the core of the racketeering activity would be immunized while the persons who worked for the enterprise could be prosecuted. *Surely Congress could not have intended such an absurd and unjust result.*" (emphasis supplied)

The Eleventh Circuit Court is in conflict also with the Circuit's adopting the "person"—"enterprise" exclusion from liability. This circuit outright repudiated this ex-

clusionary rule in *United States v. Hartley*, 678 F.2d 961 (11th Cir. 1982). The *Hartley* court stated:

> "if an individual were named as the enterprise, and a group of persons engaged in a pattern of racketeering activities with that individual, it would defy reason to suggest that the central figure (the enterprise) could not also be prosecuted under RICO."

CONCLUSION

As in the case at bar, the Tenth Circuit's decision as in countless other cases in other circuits has allowed the culpable culprit (Liberty Group—the enterprise) to conduct its illegal activities with complete impunity, contrary to the intent of Congress in enacting RICO. This is an "important issue of law" which the court must decide. Seven of the ten Circuits that have considered this issue have adopted the exception to the "person"—"enterprise" exclusionary rule. The Circuit Courts are in conflict on this issue.

WHEREFORE Petitioner respectfully prays that the Writ of Certiorari be granted.

Respectfully submitted,

J. M. DURRETT, JR.
San Juan County Attorney
112 S. Mesa Verde
Aztec, NM 87410
(505) 334-9481

JAMES L. DOW *
DOW LAW OFFICE, P.A.
P. O. Box 128
Carlsbad, NM 88221
(505) 885-2185
Attorneys for Petitioner

* Counsel of Record